

Message Text

CONFIDENTIAL

PAGE 01 ROME 12292 01 OF 03 291920Z

65

ACTION EUR-12

INFO OCT-01 ISO-00 EURE-00 AID-05 CIAE-00 COME-00 EB-07

FRB-03 INR-07 NSAE-00 XMB-02 OPIC-03 SP-02 CIEP-01

LAB-04 SIL-01 OMB-01 NSC-05 SS-15 STR-04 CEA-01

DODE-00 NSCE-00 SSO-00 USIE-00 INRE-00 IO-13 /087 W
----- 062811

O R 291800Z JUL 76

FM AMEMBASSY ROME

TO SECSTATE WASHDC IMMEDIATE 9140

TREASURY DEPT WASHDC IMMEDIATE

INFO AMEMBASSY BONN

USMISSION EC BRUSSELS

AMEMBASSY LONDON

AMCONSUL MILAN

AMCONSUL NAPLES

AMEMBASSY PARIS

USMISSION OECD PARIS

C O N F I D E N T I A L SECTION 1 OF 3 ROME 12292/1

E.O. 11652: GDS

TAGS: EFIN, IT

SUBJ: PRELIMINARY APPRAISAL OF ECONOMIC PORTION OF DRAFT
ANDREOTTI PROGRAM

TREASURY FOR WIDMAN

PASS FRB

REF: ROME 11956

SUMMARY. FOLLOWING IS EMBASSY'S INITIAL APPRAISAL OF TWO
CRITICAL ASPECTS OF ECONOMIC PORTION OF DRAFT ANDREOTTI PROGRAM:

(1) BUDGET DEFICIT AND (2) LABOR COSTS. TWIN GOALS OF REDUCING
RATIO OF PUBLIC SECTOR CURRENT EXPENDITURE DEFICIT TO GDP BY
TWO-THIRDS BY 1979 AND ELIMINATING ENTIRE CURRENT EXPENDITURE
CONFIDENTIAL

CONFIDENTIAL

PAGE 02 ROME 12292 01 OF 03 291920Z

DEFICIT IN SEVERAL YEARS ARE IMPORTANT AND APPEAR FAIRLY AMBI-

TIOUS. PROPOSALS FOR REDUCING CENTRAL GOVERNMENT EXPENDITURES ARE RATHER MODEST. SUGGESTIONS FOR INCREASING CENTRAL GOVERNMENT REVENUE ARE MORE COMPREHENSIVE BUT STILL RATHER VAGUE. IDEAS FOR RESOLVING PROBLEMS OF LOCAL GOVERNMENT FINANCE REFLECT CLEAR RECOGNITION OF IMPORTANCE OF THIS ISSUE BUT THEIR IMPLEMENTATION IS APT TO REQUIRE CONSIDERABLE TIME. PROPOSALS FOR REDUCING EXCESSIVE INCREASES IN LABOR COSTS TOUCH UPON ALL MAJOR ASPECTS OF PROBLEM BUT ARE VERY GENERAL AND CLEARLY DEPENDENT UPON COOPERATION OF LABOR UNIONS. ON BALANCE, WE BELIEVE THAT DRAFT ANDREOTTI PROGRAM ADDRESSES THE RIGHT ISSUES BUT IT IS NOT YET CLEAR WHETHER IT WILL GO FAR ENOUGH TO CORRECT ITALY'S URGENT ECONOMIC PROBLEMS. END SUMMARY.

1. BUDGET DEFICIT GOALS. THERE ARE TWIN GOALS CITED IN DRAFT ANDREOTTI PROGRAM: (1) REDUCTION IN PUBLIC SECTOR CURRENT EXPENDITURE DEFICIT AS PERCENTAGE OF GDP BY TWO-THIRDS BY 1979 AND (2) COMPLETE ELIMINATION OF SAME DEFICIT IN COURSE OF "SEVERAL YEARS." THIS DEFICIT APPARENTLY IS CONCEPTUALLY DIFFERENT FROM DEFINITION EMPLOYED BY BANK OF ITALY (BOI), IMF AND EC IN FIXING LOAN CONDITIONS BECAUSE (1) IT COVERS ALL OF PUBLIC SECTOR, BUT (2) IT COVERS ONLY CURRENT AND NOT CAPITAL OPERATIONS. BOI ANNUAL REPORT FIGURES FOR CURRENT CASH DEFICIT OF ENTIRE PUBLIC SECTOR SHOW THAT RATIO OF THIS DEFICIT TO GDP IN 1975 WAS 5.3 PERCENT. (THIS COMPARES WITH ABOUT 12.5 PERCENT RATIO FOR CASH DEFICIT UNDER BOI/IMF/EC DEFINITIONS.) THUS, GOAL WOULD REDUCE THIS RATIO TO ABOUT 1.7 PERCENT BY 1979. TABLES 1A AND 1B BELOW SHOW EMBASSY ESTIMATES OF RATIO OF THIS DEFICIT TO ROUGHLY ESTIMATED GDP IN CURRENT LIRE FOR PERIOD 1976-1981.

TABLE 1A

PUBLIC SECTOR CASH DEFICIT/GDP RATIO
(BILLIONS OF LIRE, PERCENT)

	1975	1976E	1977E	1978E	1979E
CURRENT OPERATIONS DEFICIT	-5,907	-7,289	-7,074	-5,296	-3,292
GDP	112,358	137,526	157,192	176,527	193,650
PERCENT	5.3	5.3	4.5	3.0	1.7

E - ESTIMATE

SOURCE: 1975 BANK OF ITALY ANNUAL REPORT

RATIO OF DEFICIT FOR 1976 IS ASSUMED UNCHANGED FROM 1975.

DEFICITS FOR 1977 AND 1978 ARE CALCULATED ON BASIS OF ARBITRARY
CONFIDENTIAL

CONFIDENTIAL

PAGE 03 ROME 12292 01 OF 03 291920Z

RATIOS OF 4.5 AND 3.0 PERCENT, ASSUMING GRADUAL REDUCTION IN RATIO OF DEFICIT TO GDP IN ORDER TO REACH 1979 GOAL.

2. SECOND PART OF BUDGET DEFICIT GOAL IS TO COMPLETELY ELIMINATE PUBLIC SECTOR CURRENT EXPENDITURE DEFICIT IN "SEVERAL YEARS." IF THIS WERE INTERPRETED TO BE ELIMINATION OF RESIDUAL DEFICIT BY 1981, PATTERN WOULD BE APPROXIMATELY AS SHOWN IN TABLE 1B.

TABLE 1B
PUBLIC SECTOR CASH DEFICIT/GDP RATIO
(BILLIONS OF LIRE, PERCENT)

	1980E	1981E
CURRENT OPERATIONS DEFICIT	-1,704	-
GDP	213,015	234,316
PERCENT	0.8	-

E-ESTIMATE

PURPOSE OF THIS GOAL IS FIRST TO ELIMINATE DEFICIT AND THEN TO CREATE SURPLUS IN CURRENT EXPENDITURES TO HELP FINANCE RISE IN CAPITAL EXPENDITURES FOR PUBLIC INVESTMENT. (NOTE THAT ANOTHER GOAL IN ANDREOTTI PROGRAM IS TO INCREASE INVESTMENT IN PUBLIC WORKS TO 5 OR 6 PERCENT OF GDP COMPARED TO 3 PERCENT IN RECENT YEARS.)

3. REDUCTION IN BUDGET EXPENDITURES. QUESTION OF WHETHER EMPHASIS IN REDUCING BUDGET DEFICIT SHOULD BE ON INCREASING REVENUES OR ON REDUCING EXPENDITURES HAS BEEN SUBJECT OF DEBATE IN ITALY. DATA SHOW THAT ITALIAN EXPENDITURE LEVELS COMPARED TO GDP ARE NOT VERY DIFFERENT FROM AVERAGE LEVELS IN OTHER EC COUNTRIES, BUT THAT RATIO OF REVENUES TO GDP IS SIGNIFICANTLY LOWER IN ITALY, DRAFT PROGRAM EXPRESSES SKEPTICISM ABOUT GOI ABILITY TO REDUCE BUDGET EXPENDITURES IN REAL TERMS OR TO REDUCE RATIO OF EXPENDITURES TO GDP BECAUSE OF SUCH FACTORS AS: INDEXATION OF SALARIES AND PENSIONS, EXISTING MULTI-YEAR EXPENDITURE PROGRAMS AND PROPOSED CONSOLIDATION OF LOCAL GOVERNMENT DEBT.

MAIN EFFORT ON EXPENDITURE SIDE WOULD BE TO ARREST RATE OF INCREASE IN EXPENDITURES, INCLUDING A TEMPORARY FREEZE ON WAGE AND COST OF LIVING INCREASES AT HIGH INCOME LEVELS.

4. EMBASSY BELIEVES THAT EFFORT MUST BE MADE BOTH TO REDUCE EXPENDITURES AND TO RAISE REVENUES. RELATIVE IMPORTANCE ASSIGNED
CONFIDENTIAL

CONFIDENTIAL

PAGE 04 ROME 12292 01 OF 03 291920Z

TO TWO APPROACHES IS LESS IMPORTANT THAN IS NEED TO ACT PROMPTLY TO REDUCE DEFICIT. HISTORICAL DATA IN TABLE 2 SUGGEST THAT RATIO OF CENTRAL GOVERNMENT REVENUES TO GDP HAS REMAINED CONSTANT AT LEAST UNTIL 1975, WHILE EXPENDITURE TO GDP RATIO HAS RISEN SIGNIFICANTLY. (CASH REVENUE AND EXPENDITURE DATA FOR PUBLIC SECTOR ARE NOT READILY AVAILABLE FOR LONG ENOUGH PERIOD TO SHOW USEFUL TREND.) ON REVENUE SIDE, IT IS STILL DIFFICULT TO EVALUATE EFFECTS OF 1973/75 TAX REFORM. HOWEVER, INCREASE IN REVENUE TO GDP RATIO IN 1975 IS ENCOURAGING. AT SAME TIME, RISE INEXPENDITURE TO GDP RATIO IN 1975 MAY BE TEMPORARY PHENOMENA DUE TO RISE IN TRANSFER PAYMENTS DURING PERIOD OF RECESSION. ON BALANCE, EMBASSY BELIEVES THAT, PARTICULARLY IN SHORT RUN, MAIN EFFORT TO REDUCE BUDGET DEFICIT MUST BE MADE ON REVENUE SIDE TAHOUGH AT LEAST TEMPORARY TAX RATE INCREASES WHICH WOULD BE IMMEDIATELY EFFECTIVE. IN LONGER RUN, THERE

CONFIDENTIAL

NNN

CONFIDENTIAL

PAGE 01 ROME 12292 02 OF 03 291903Z

44

ACTION EUR-12

INFO OCT-01 ISO-00 EURE-00 AID-05 CIAE-00 COME-00 EB-07

FRB-03 INR-07 NSAE-00 XMB-02 OPIC-03 SP-02 CIEP-01

LAB-04 SIL-01 OMB-01 NSC-05 SS-15 STR-04 CEA-01

DODE-00 NSCE-00 SSO-00 USIE-00 INRE-00 IO-13 /087 W

----- 062579

O R 291800Z JUL 76

FM AMEMBASSY ROME

TO SECSTATE WASHDC IMMEDIATE 9141

TREASURY DEPARTMENT WASHDC IMMEDIATE

INFO AMEMBASSY BONN

USMISSION EC BRUSSELS

AMEMBASSY LONDON

AMCONSUL MILAN

AMCONSUL NAPLES

AMEMBASSY PARIS

USMISSION OECD PARIS

C O N F I D E N T I A L SECTION 2 OF 3 ROME 12292

TREASURY FOR WIDMAN

PASS FRB

IS MORE HOPE THAT RATE OF GROWTH IN EXPENDITURES CAN BE REDUCED AND THAT TAX COLLECTION SYSTEM CAN BE IMPROVED.

TABLE 2

RATIO TO GDP: CENTRAL GOVT CASH REVENUES AND EXPEND.

	1969	1970	1971	1972	1973	1974	1975
REVENUES	18.3	18.3	18.8	17.8	17.4	18.6	21.3
EXPENDITURES	19.5	22.5	23.6	23.0	26.3	23.8	30.4

5. SPECIFIC PROPOSAL FOR TEMPORARY FREEZE ON HIGH INCOME LEVELS CONTAINED IN DRAFT PROGRAM, EVEN THOUGH CONTAINED IN SECTION DEALING WITH PUBLIC EXPENDITURES, SEEMS TO REFER TO TEMPORARY FREEZE OF WAGES AND COST OF LIVING ADJUSTMENTS FOR

CONFIDENTIAL

CONFIDENTIAL

PAGE 02 ROME 12292 02 OF 03 291903Z

BOTH PUBLIC AND PRIVATE HIGH-LEVEL WAGE AND SALARIED EMPLOYEES ("DEPENDENT LABOR"). LABOR UNIONS HAVE ALREADY EXPRESSED WILLINGNESS TO CONSIDER THIS TYPE OF APPROACH AND HAVE MENTIONED CUTOFF AT 8 MILLION LIRE (ABOUT \$9600). (HOWEVER, THEY HAVE SUGGESTED THAT SAVINGS BE CHANNELLED INTO PRODUCTIVE INVESTMENT.) WHILE GOOD DATA ON DISTRIBUTION OF INCOME IN ITALY ARE NOT READILY AVAILABLE, EMBASSY BELIEVES THAT CUTOFF AT THAT HIGH A LEVEL WOULD ONLY AFFECT ABOUT 10 PERCENT OF DEPENDENT LABOR. HISTORIC DATA ON CASH BUDGET CURRENT OPERATIONS OF PUBLIC SECTOR SHOW THAT WAGES AVERAGED 33 PERCENT OF TOTAL CURRENT EXPENDITURES IN PERIOD 1972-75. TEMPORARY WAGE FREEZE AFFECTING ONLY 10 PERCENT OF PUBLIC SECTOR WAGE EARNERS WOULD HAVE HELPFUL, BUT RATHER MODEST, EFFECT IN REDUCING DEFICIT. FOR EXAMPLE, IF WAGE RATES IN PUBLIC SECTOR WERE TO INCREASE IN 1976 BY 10 PERCENT BUT INCREASE ONLY APPLIED TO 90 PERCENT OF GOVERNMENT EMPLOYEES, THERE WOULD BE SAVINGS OF ONLY ABOUT 140 BILLION LIRE. IF SALARY CUTOFF LEVEL COULD BE LOWERED, THIS COULD HAVE MORE PERCEPTIBLE IMPACT ON WAGE COSTS IN PUBLIC SECTOR.

6. PERHAPS MORE EFFECTIVE WAY FOR CUTTING BACK EXPENDITURES MIGHT BE TO EXTEND DRAFT PROGRAM'S PROPOSED FREEZE ON HIRING AT LOCAL GOVERNMENT LEVEL TO CENTRAL GOVERNMENT AS WELL. SAVINGS WOULD THEN COME ABOUT THROUGH ATTRITION.

7. DRAFT PROGRAM ALSO REFERS TO CONTROL OVER EXPLOSION OF HEALTH EXPENDITURES AND CITES CERTAIN PRACTICES PREVALENT ABROAD (E.G., EXHORTATION AGAINST EXCESSIVE USE OF FREE MEDICINES AND SHORTER PAID HOSPITALIZATION WHICH MIGHT BE COPIED IN ITALY.

8. INCREASE IN BUDGET REVENUES. MAIN ITEMS IN DRAFT PROGRAM ARE PROPOSALS FOR INCREASES IN PUBLIC SERVICE TARIFFS, SELECTIVE AUDITS OF TAX RETURNS, INCREASE IN TAX BASE UPON WHICH TAXES ON CAPITAL GAINS AND REAL ESTATE ARE ASSESSED, INCREASE IN VALUE ADDED TAX (VAT) ON NON-ESSENTIAL GOODS, AND INCREASE IN INCOME TAX RATES AT MIDDLE AND UPPER LEVELS. ALL OF THESE MEASURES ALTHOUGH NOT YET QUANTIFIABLE, COULD BE IMPORTANT.

9. DRAFT PROGRAM PROPOSES THAT CENTRAL GOVERNMENT CONTRIBUTION TO FINANCE PUBLIC SERVICES BE LIMITED TO FINANCING OF

CONFIDENTIAL

CONFIDENTIAL

PAGE 03 ROME 12292 02 OF 03 291903Z

INVESTMENT EXPENDITURES, EXCEPT FOR LIMITED COVERAGE OF CUR-

RENT EXPENDITURE DEFICITS IN TRANSPORT SECTOR. ELECTRICITY ENTITY (ENEL) IS ALREADY COMMITTED TO TARIFF INCREASES AS PART OF ITS PLAN TO FINANCE ITS NUCLEAR ENERGY PROGRAM. ALTHOUGH NOT SPECIFICALLY MENTIONED IN DRAFT PROGRAM, WE HOPE EFFORT WILL BE MADE TO INCREASE BOTH URBAN TRANSPORT AND NATIONAL RAILROAD FARES. THESE TWO MEASURES WOULD REDUCE CASH DEFICIT IN FORM OF REDUCED CAPITAL ENDOWMENT CONTRIBUTIONS TO ENEL, REDUCED TRANSFERS TO AUTONOMOUS AGENCIES (THE RAILROADS) AND REDUCED FINANCING OF LOCAL GOVERNMENT DEFICITS.

10. PROPOSAL FOR SELECTIVE AUDITS BASED ON COMPUTERIZED TAX RATES IS AIMED AT CONCENTRATING AVAILABLE MANPOWER ON EXAMINING SELECTED TAX CASES RATHER THAN ON PROCESSING BULK OF TAX RETURNS, AS IS NOW THE CASE. ALTHOUGH COMPUTER SYSTEM IS STILL NOT YET IN OPERATION, MINISTER OF FINANCE HAS ALREADY PROPOSED TO BEGIN SELECTIVE AUDITS IN SEPTEMBER.

11. PROPOSAL FOR INCREASING TAX BASE FOR TAXING CAPITAL GAINS AND REAL ESTATE IS NOT YET CLEAR. AT PRESENT, CAPITAL GAINS ARE TAXED THE SAME AS ORDINARY INCOME, WHILE TAXES ON IMPUTED INCOME FROM REAL ESTATE ARE ASSESSED AT ARTIFICIALLY LOW CADASTRAL VALUATION. THERE HAS BEEN SOME PUBLIC DISCUSSION OF INTRODUCING LOCAL PROPERTY TAX ON REAL ESTATE. ALSO, EXISTING TRANSFER TAX ON INCREASED VALUE OF REAL ESTATE, INVIM, IS CURRENTLY BEING CRITICIZED AS A POOR GENERATOR OF REVENUE.

12. AS TO TAX RATE INCREASES, PROPOSAL FOR FURTHER RISES IN VAT ON NON-ESSENTIAL GOODS (ESPECIALLY IMPORTS) MAY HAVE MORE PSYCHOLOGICAL THAN REVENUE EFFECT, SINCE RATES ARE ALREADY RATHER HIGH ON A NUMBER OF SUCH ITEMS, PARTICULARLY AS RESULT OF MARCH 1976 VAT RATE INCREASES. MORE PROMISING IS PROPOSAL TO RAISE PERSONAL INCOME TAX RATES AT MIDDLE AND UPPER LEVELS TO AVERAGE EC RATES. (IN 1975, 21 PERCENT OF CENTRAL GOVERNMENT CASH REVENUES WERE GENERATED BY THE PERSONAL INCOME TAX.) PROPOSAL HAS NOT YET BEEN QUANTIFIED, BUT IF RATE INCREASES ARE ASSESSED FAR ENOUGH DOWN IN WAGE PYRAMID, MEASURE COULD GENERATE SUBSTANTIAL AMOUNT OF NEW REVENUE AND WOULD REVERSE BADLY-TIMED REDUCTION IN INCOME TAX RATES ADOPTED IN DECEMBER 1975 TO FIGHT "FISCAL DRAG."

CONFIDENTIAL

CONFIDENTIAL

PAGE 04 ROME 12292 02 OF 03 291903Z

13. LOCAL GOVERNMENT FINANCE. DRAFT PROGRAM CONTAINS SERIES OF PROPOSALS IN HIGHLY COMPLEX FIELD OF LOCAL GOVERNMENT FINANCE ("ENTI TERRITORIALI" WHICH ESSENTIALLY CONSIST OF MUNICIPAL, PROVINCIAL AND REGIONAL GOVERNMENTS.) WHICH OVER LONG RUN COULD HAVE IMPORTANT EFFECT ON REDUCING OVERALL CASH BUDGET DEFICIT. PERHAPS MOST IMPORTANT PROPOSAL IS PLAN TO RESTORE LIMITED TAX AUTONOMY--WITHOUT SPECIFYING WHAT TAXES-- TO LOCAL GOVERNMENTS TO PERMIT THEM TO FINANCE ONE-THIRD OF

THEIR EXPENDITURES FROM THEIR OWN REVENUES. TABLE 4 SHOWS DATA FROM BOI ANNUAL REPORT FOR PERIOD 1973-1975 WHICH INDICATE THAT IN 1975 ONLY ABOUT 10 PERCENT OF LOCAL GOVERNMENT EXPENDITURES WERE COVERED BY LOCAL TAX REVENUES. IF ONE-THIRD OF EXPENDITURES HAD BEEN SO FINANCED, LOCAL TAX REVENUES WOULD HAVE HAD TO BE MORE THAN THREE TIMES ACTUAL LEVEL OR, IN ABSOLUTE AMOUNT, ALMOST 2,700 BILLION LIRE HIGHER. (NOTE, HOWEVER, THAT RECENT PATTERN OF SHARP DECLINE IN TAX TO EXPENDITURE RATIO FOR LOCAL GOVERNMENT IS DUE TO DELIBERATE TRANSFER OF EXPENDITURE AUTHORITY TO REGIONAL GOVERNMENTS WHILE SIMULTANEOUSLY, THROUGH TAX REFORM, ELIMINATING MOST LOCAL TAXING AUTHORITY AND SUBSTITUTING REVENUE-SHARING. PERNICIOUS EFFECTS OF DISASSOCIATING TAXING AND SPENDING AUTHORITY WOULD BE PARTLY ELIMINATED BY RESTORING LIMITED TAXING POWER TO LOCAL GOVERNMENTS.

CONFIDENTIAL

NNN

CONFIDENTIAL

PAGE 01 ROME 12292 03 OF 03 291935Z

54

ACTION EUR-12

INFO OCT-01 ISO-00 EURE-00 TRSE-00 AID-05 CIAE-00 COME-00

EB-07 FRB-03 INR-07 NSAE-00 XMB-02 OPIC-03 SP-02

CIEP-01 LAB-04 SIL-01 OMB-01 NSC-05 SS-15 STR-04

CEA-01 DODE-00 NSCE-00 SSO-00 USIE-00 INRE-00 IO-13

/087 W

----- 063022

O R 291800Z JUL 76

FM AMEMBASSY ROME

TO SECSTATE WASHDC IMMEDIATE 9142

TREASURY DEPARTMENT WASHDC IMMEDIATE

INFO AMEMBASSY BONN

USMISSION EC BRUSSELS

AMEMBASSY LONDON

AMCONSUL NAPLES

AMCONSUL MILAN

AMEMBASSY PARIS

USMISSION OECD PARIS

C O N F I D E N T I A L SECTION 3 OF 3 ROME 12292

TREASURY FOR WIDMAN

PASS FRB

TABEL 4

LOCAL GOVERNMENT TAX REVENUE (CASH BASIS)					
	1973	1974	1975	1975(THEOR)	
TAX REVENUES	1,535	1,071	1,132	3,800	
TOTAL EXPENDITURES					
(CORP.PLUS CAPITAL)	6,381	8,130	11,514	11,514	
TAX/EXPEND. RATIO	24.1	13.2	9.8	33.0	

SOURCE: BANK OF ITALY ANNUAL REPORT 1975

CONFIDENTIAL

CONFIDENTIAL

PAGE 02 ROME 12292 03 OF 03 291935Z

14. EXCEPT FOR PROPOSED THREE-YEAR FREEZE ON HIRING, WHICH COULD BE RATHER IMPORTANT MEANS OF CONTROLLING GROWTH OF LOCAL GOVERNMENT EXPENDITURES, MOST OF REMAINING PROPOSALS CONSTITUTE PACKAGE DESIGNED TO CLEAR UP ACCUMULATED LOCAL GOVERNMENT DEBT PROBLEM WHILE CREATING NEW MECHANISM FOR EXERCISING TIGHTER CONTROL OVER EXPENDITURES. CENTRAL GOVERNMENT HAS ALREADY ASSUMED SOME RESPONSIBILITY FOR CONSOLIDATION OF LOCAL GOVERNMENT DEBT IN RECENT YEARS. FURTHER CONSOLIDATION OF LOCAL DEBT MAY BE JUSTIFIED ONLY IF IT IS LINKED TO EFFECTIVE CONTROL OVER ACCUMULATION OF NEW DEBT.

15. NEW COORDINATING BODY WOULD BE CREATED TO FIX AMOUNTS AND USE OF CENTRAL GOVERNMENT TRANSFERS TO LOCAL GOVERNMENTS. DECISIONS WOULD TAKE INTO ACCOUNT AVAILABLE RESOURCES, OVERALL ECONOMIC POLICY AND PROPER FUNCTIONS OF LOCAL GOVERNMENTS. THIS SHOULD IMPROVE CONTROL OVER SUCH TRANSFERS, WHICH HAVE BECOME INCREASINGLY IMPORTANT DUE TO REASSIGNMENT OF MANY GOVERNMENT RESPONSIBILITIES FROM CENTRAL GOVERNMENT TO REGIONAL AND OTHER LOCAL GOVERNMENTS. PROPOSAL FOR CONCENTRATION OF CREDITS TO LOCAL GOVERNMENTS IN SINGLE BODY SEEMS DESIGNED TO ASSURE THAT SUCH CREDITS ARE ONLY GRANTED FOR AGREED-UPON PURPOSES.

16. LABOR COSTS. DRAFT PROGRAM CONTAINS VERY LITTLE DETAIL ON WAY IN WHICH RISE IN LABOR COSTS WOULD BE LIMITED. APPARENTLY, THIS MATTER WOULD BE DEALT WITH MAINLY THROUGH DIRECT NEGOTIATIONS WITH LABOR UNIONS. PROPOSAL FOR A TEMPORARY FREEZE ON WAGE AND COST OF LIVING RISES ABOVE CERTAIN INCOME LEVELS (SEE PARA 3) COULD BE IMPORTANT IF CUTOFF WERE REDUCED BELOW 8 MILLION LIRE PER YEAR FIGURE MENTIONED BY LABOR UNIONS. FOR EXAMPLE, DC ECONOMISTS HAVE SUGGESTED CUTOFF OF 5 MILLION LIRE. REDUCTION IN CUTOFF TO THAT LEVEL WOULD APPARENTLY COVER AT LEAST 20 PERCENT OF LABOR FORCE, RATHER THAN 10 PER-

CENT AT HIGHER CUTOFF LEVEL. SERIOUS EFFORT SHOULD BE MADE BY GOI TO LOWER CUTOFF LEVEL, AND IT IS EMBASSY'S IMPRESSION THAT UNION LEADERS MAY BE PREPARED TO ACCEPT SOME COMPROMISE IN THIS AREA.

17. REMAINING REFERENCES TO LABOR COST PROBLEM CONSIST OF RECOGNITION OF NEED FOR BUSINESS AND LABOR TO TAKE INTO ACCOUNT EFFECT ON INVESTMENT AND EMPLOYMENT DURING COLLECTIVE BAR-
CONFIDENTIAL

CONFIDENTIAL

PAGE 03 ROME 12292 03 OF 03 291935Z

GAINING PROCESS. IN FACT, IN RECENT YEARS, AT LEAST UNTIL LATEST ROUND OF CONTRACT NEGOTIATIONS, LABOR UNIONS HAVE PAID LITTLE ATTENTION TO EVENTUAL IMPACT ON EMPLOYMENT OF EXCESSIVE WAGE RATE INCREASES. HOWEVER, IN LAST NINE MONTHS OR SO NATIONAL UNION LEADERSHIP HAS PUBLICLY STRESSED THAT PRIORITY IN CONTRACT NEGOTIATIONS MUST BE GIVEN TO EMPLOYMENT RATHER THAN WAGE RATES. OTHER ASPECTS OF LABOR COSTS, I.E., WAGE RATE INDEXATION, WAGE SUPPLEMENT FUND FOR SHORT-TIME WORK, UNEMPLOYMENT INSURANCE PROGRAM, LABOR IMMOBILITY, ABSENTEEISM AND EXCESSIVE NUMBER OF HOLIDAYS (PARTICULARLY INTRA-WEEK HOLIDAYS) ARE ALL MENTIONED IN DRAFT PROGRAM AS SUBJECT FOR DISCUSSION BETWEEN GOI AND LABOR LEADERS. EXCEPT FOR WILLINGNESS TO TEMPORARILY FREEZE COST OF LIVING ADJUSTMENT AT HIGH WAGE LEVELS, UNIONS HAVE BEEN QUITE RETICENT ABOUT TAMPERING WITH INDEXATION. THEY HAVE, ON THE OTHER HAND, INDICATED WILLINGNESS TO DISCUSS DIRECTLY WITH BUSINESS WAYS OF INCREASING LABOR MOBILITY, REDUCING ABSENTEEISM AND ELIMINATING INTRA-WEEK HOLIDAYS BY ADDING EQUAL AMOUNT OF TIME TO REGULAR VACATION PERIODS.

18. COMMENT. IT SHOULD BE BORNE IN MIND THAT DRAFT ANDREOTTI PROGRAM DOES NOT PURPORT TO BE, NOR CAN IT BE AT THIS STAGE, A DETAILED STABILIZATION PLAN OF TYPE WHICH MUST ULTIMATELY BE PREPARED IF ITALY IS TO OBTAIN FOREIGN CREDITS FROM IMF AND OTHER LENDERS. DRAFT PROGRAM IS NECESSARILY RATHER VAGUE ON MANY ISSUES. AFTER GOVERNMENT IS FORMED, MORE DETAILED PROGRAM WILL HAVE TO BE DEVELOPED, IN MANY CASES INVOLVING COMPLEX NEGOTIATIONS WITH LABOR UNIONS AND PREPARATION AND SUBMISSION OF SPECIFIC LEGISLATIVE PROPOSALS TO PARLIAMENT.

19. IN THESE CIRCUMSTANCES, IT IS DIFFICULT TO APPRAISE ADEQUACY OF PROPOSALS. DRAFT PROGRAM DOES IDENTIFY ESSENTIAL PROBLEMS AND TOUCHES UPON VARIOUS WAYS IN WHICH THEY MIGHT BE DEALT WITH. THIS IS ENCOURAGING EVIDENCE OF EXTENT TO WHICH POLITICAL AND LABOR LEADERS HAVE COME TO RECOGNIZE SERIOUSNESS OF ITALY'S ECONOMIC PROBLEMS. ALSO, EMBASSY DOES NOT BELIEVE THAT GOI LEADERS HAVE ANY ILLUSIONS THAT PRESENT DRAFT PROGRAM WOULD PROVIDE ADEQUATE GROUNDS FOR SEEKING FOREIGN CREDITS. EMBASSY HAS BEEN ASSURED (BY TREASURY DIRECTOR GENERAL PALUMBO) THAT DRAFTERS OF ANDREOTTI PROGRAM WERE

FULLY AWARE OF STATUS OF STANDBY NEGOTIATIONS BETWEEN GOI AND
CONFIDENTIAL

CONFIDENTIAL

PAGE 04 ROME 12292 03 OF 03 291935Z

IMF AND OF TYPES OF CONDITIONS LIKELY TO BE ATTACHED TO FUTURE
FOREIGN CREDITS FROM IMF, EC OR OTHER POTENTIAL LENDERS. IT
IS NOT CLEAR TO EMBASSY HOW OR AT WHAT STAGE POTENTIAL FOREIGN
LENDERS WILL HAVE OPPORTUNITY FOR DIRECT CONTACT WITH NEW
GOVERNMENT TO EVALUATE SPECIFIC ECONOMIC POLICY CONDITIONS FOR
ANY NEW LOANS. HOWEVER, EVERY EFFORT MUST BE MADE TO ENCOURAGE
GOI TO FLESH OUT PROGRAM AS SOON AS POSSIBLE TO ASSURE THAT
PROGRAM IS SUFFICIENTLY RIGOROUS IN ITS INITIAL VERSION SO
THAT ANY POLITICAL COMPROMISES WHICH MAY HAVE TO BE MADE
INSIDE OR OUTSIDE PARLIAMENT CAN BE ACCEPTED WITHOUT GUTTING
PROGRAM. VOLPE

CONFIDENTIAL

NNN

Message Attributes

Automatic Decaptioning: X
Capture Date: 01 JAN 1994
Channel Indicators: n/a
Current Classification: UNCLASSIFIED
Concepts: REPORTS, ECONOMIC PROGRAMS, FINANCIAL PROGRAMS
Control Number: n/a
Copy: SINGLE
Draft Date: 29 JUL 1976
Decaption Date: 01 JAN 1960
Decaption Note:
Disposition Action: RELEASED
Disposition Approved on Date:
Disposition Authority: ShawDG
Disposition Case Number: n/a
Disposition Comment: 25 YEAR REVIEW
Disposition Date: 28 MAY 2004
Disposition Event:
Disposition History: n/a
Disposition Reason:
Disposition Remarks:
Document Number: 1976ROME12292
Document Source: CORE
Document Unique ID: 00
Drafter: n/a
Enclosure: n/a
Executive Order: GS
Errors: N/A
Film Number: D760293-0866
From: ROME
Handling Restrictions: n/a
Image Path:
ISecure: 1
Legacy Key: link1976/newtext/t1976079/aaaaahkz.tel
Line Count: 511
Locator: TEXT ON-LINE, ON MICROFILM
Office: ACTION EUR
Original Classification: CONFIDENTIAL
Original Handling Restrictions: n/a
Original Previous Classification: n/a
Original Previous Handling Restrictions: n/a
Page Count: 10
Previous Channel Indicators: n/a
Previous Classification: CONFIDENTIAL
Previous Handling Restrictions: n/a
Reference: 76 ROME 11956
Review Action: RELEASED, APPROVED
Review Authority: ShawDG
Review Comment: n/a
Review Content Flags:
Review Date: 05 APR 2004
Review Event:
Review Exemptions: n/a
Review History: RELEASED <05 APR 2004 by greeneet>; APPROVED <12 AUG 2004 by ShawDG>
Review Markings:

Margaret P. Grafeld
Declassified/Released
US Department of State
EO Systematic Review
04 MAY 2006

Review Media Identifier:
Review Referrals: n/a
Review Release Date: n/a
Review Release Event: n/a
Review Transfer Date:
Review Withdrawn Fields: n/a
Secure: OPEN
Status: NATIVE
Subject: PRELIMINARY APPRAISAL OF ECONOMIC PORTION OF DRAFT ANDREOTTI PROGRAM TREASURY FOR WIDMAN
TAGS: EFIN, IT, (ANDREOTTI)
To: STATE TRSY
Type: TE
Markings: Margaret P. Grafeld Declassified/Released US Department of State EO Systematic Review 04 MAY 2006